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IN THE UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
RICHMOND DIVISION

In re:	:	Chapter 11
	:	
CIRCUIT CITY STORES, INC., et al.,	:	Case No. 08-35653 (KRH)
	:	
	:	Jointly Administered
Debtors.	:	

DEBTORS' OMNIBUS REPLY IN SUPPORT OF (I) FIFTY-SECOND OMNIBUS OBJECTION TO CERTAIN 503(b)(9) CLAIMS AND (II) MOTION FOR A WAIVER OF THE REQUIREMENT THAT THE FIRST HEARING ON ANY RESPONSE PROCEED AS A STATUS CONFERENCE

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PRELIMINARY STATEMENT

By the Objection,[1] the Debtors seek temporary disallowance of the 503(b)(9) Claims because the Claimants holding such Claims received transfers avoidable under Bankruptcy Code section 547. In an effort to ease the administrative burden on this Court and provide affected creditors with the opportunity to participate in the resolution of common legal issues, the Debtors also request that this Court bifurcate the hearing on the Objection.

Specifically, the Debtors request that this Court resolve any common legal issues at the hearing on November 12 (the "Hearing") and reserve any factual issues for subsequent hearings with respect to each Claimant that responded (each a "Respondent", collectively, the "Respondents", and their responses collectively, the "Responses"). Only after each such subsequent hearing would the Court enter an order sustaining or overruling the Objection. In the Debtors' view, this process protects the Claimants' rights. Many Respondents objected to this

[1] Capitalized terms not otherwise defined herein shall have the meanings ascribed to them in the Debtors' Brief In Support Of Debtors' (I) Fifty-Second Omnibus Objection To Certain 503(b)(9) Claims and (II) Motion For A Waiver Of The Requirement That The First Hearing On Any Response Proceed As A Status Conference (the "Opening Brief").

proposed process, arguing that the process violates their due process rights and that the Debtors were required to commence an adversary proceeding to obtain the relief requested in the Objection.

As demonstrated herein, the proposed process of bifurcating legal and factual issues (i) satisfies constitutional due process, (ii) presents justiciable issues properly considered by the Court and does not constitute a request for an advisory opinion, and (iii) is a cost effective mechanism accepted by other bankruptcy courts facing similar issues. Moreover, because the Debtors are not requesting any affirmative relief, i.e., the recovery of money or property or a declaration, but simply a ruling on threshold legal issues in a form similar to seeking partial summary judgment, they were not required to commence an adversary proceeding. Consequently, the Respondents' procedural objections should be overruled and this Court may proceed to decide the threshold legal issues presented by the Objection, Reponses, and this reply (the "Reply").[2]

[2] By this Reply, the Debtors have attempted to address all issues that are ripe for consideration at the Hearing. To the extent the Debtors have not specifically addressed an argument in this Reply, *(cont'd)*

THRESHOLD LEGAL ISSUES[3]

To assist the Court and the Respondents, the Debtors have identified the following four threshold legal issues, which include the procedural objections raised by the Respondents, that should be resolved at the Hearing:

I. Issue: Whether this Court may bifurcate the hearing and resolve common legal issues prior to making findings of fact with respect to the specific claims of a Respondent?

Respondents' Position: Bifurcating the hearing violates the Respondents' due process rights and a decision by the Court violates Article 2 of the Constitution because the Debtors are requesting an advisory opinion.

Debtors' Position: The process proposed by the Debtors (i) protects the Respondents' due process rights because their right to a subsequent individual judicial determination is preserved, (ii) is not a request for an advisory opinion because there is a justiciable case and controversy and, thus, in essence a request for partial summary judgment proper in the context of a contested matter under Bankruptcy Rule 9014, and (iii) has been used by other bankruptcy courts to address similar disputes. Accordingly,

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the Debtors reserve the right to address such argument at the Hearing or in supplemental submissions. Nothing herein shall constitute a waiver of such rights. All rights are expressly reserved.

[3] This section is intended as a summary of the legal issues presented by the Objection, the Responses and this Reply, as well as the general position of the various Respondents and the Debtors' position. The "Respondents' Position" may vary somewhat from Respondent to Respondent and not all Respondents presented all of the arguments addressed herein.

the Court may properly bifurcate the hearing on the Objection and address common legal issues prior to resolving factual disputes.

II. Issue: Whether the Debtors were required to commence an adversary proceeding?

Respondents' Position: The Debtors are seeking to avoid allegedly preferential transfers, i.e., to recover money or property, which must proceed by adversary proceeding.

Debtors' Position: Section 502(d) is a defense that may be raised by claim objection, and the Debtors need not proceed in an adversary proceeding. In that regard, the Debtors are not seeking to affirmatively recover money or property nor are they seeking a declaration regarding any such recovery. Instead, the Debtors are seeking a ruling on threshold legal issues similar to seeking partial summary judgment in the context of a claims objection under Bankruptcy Rule 3007 and a contested matter governed by Bankruptcy Rule 9014. Thus, it was not necessary for the Debtors to commence an adversary proceeding under Bankruptcy Rule 7001.

III. Issue: Whether the Debtors may invoke section 502(d) to temporarily disallow the 503(b)(9)?

Respondents' Position: Section 502(d) cannot be invoked to temporarily disallow 503(b)(9) Claims because the 503(b)(9) Claims are administrative expenses to which section 502(d) does not apply.

Debtors' Position: Section 502(d) applies to any claim, not just pre-petition claims or claims for which a proof of claim must be filed, including the 503(b)(9) Claims.

IV. Issue: Whether the Debtors may invoke section 502(d) to temporarily disallow 503(b)(9) Claims based upon a prima facie showing that the Respondents received transfers avoidable under section 547?

Respondents' Position: The Debtors may not invoke Section 502(d) because the Debtors have not obtained a judgment in an avoidance action that the Respondents are liable for receipt of a preferential transfer.

Debtors' Position: The Debtors may invoke section 502(d) upon making a prima facie showing that the Respondents received a transfer avoidable under section 547.

ARGUMENT

I. THIS COURT MAY BIFURCATE THE HEARING AND RESOLVE COMMON LEGAL ISSUES PRIOR TO MAKING FINDINGS OF FACT WITH RESPECT TO EACH RESPONDENT.

In the Objection, the Debtors requested that this Court bifurcate the hearing on the Objection to address threshold legal issues at the first hearing, leaving factual issues for any subsequent hearings after discovery. Certain Respondents object to this request arguing that it denies them due process and that any decision rendered at the first hearing would constitute an advisory opinion.[4] The Respondents' arguments should be rejected on four grounds.

[4] See Response of LG Electronics USA, Inc. ("LG") (D.I. 5489) at p. 4-5; Response of Samsung Electronics Corp. ("Samsung") (D.I. 5500) at p. 33; Reponse of Paramount Home Entertainment ("Paramount") (D.I. 5434) at p. 14; Response of Pioneer Electronics USA, Inc. ("Pioneer") (D.I. 5464) at p. 5.

First, the bifurcated hearing process does not deny the Respondents' due process rights. The Fourth Circuit Court of Appeals has recognized that due process is not a "technical conception of inflexible procedures." A.H. Robins Co. v. Piccinin, 788 F.2d 994, 1014 (4th Cir. 1986) (internal quotation omitted). "[R]ather, [it is] a delicate process of adjustment and of a balancing of interests in which it is recognized that what is unfair in one situation may be fair in another." Id. (internal quotations omitted). Moreover, when a dispute involves property rights only, "mere postponement of the judicial inquiry is not a denial of due process, if the opportunity given for ultimate judicial determination . . ." is preserved. Id. (citing Parratt v. Taylor, 451 U.S. 527, 540 (1981)).

Here, the Debtors are proposing a two-step adjudication process whereby, first, the Court addresses threshold legal issues common to all Respondents, and, second, the Court may hold subsequent hearings to address factual issues that may be unique to a Respondent. Thus, no "ultimate judicial determination" is made without a Respondent receiving adequate notice and an opportunity to

be heard on all issues. Consequently, there is simply no due process violation.

Second, this Court is not being asked to render an advisory opinion by resolving the threshold legal issues presented by the Objection and Responses. Specifically, the Court would be issuing an advisory opinion if the Court were being asked to render a decision based on hypothetical facts, or to address abstract issues lacking a concrete factual basis. See In re Nixon, 2007 WL 1394033, *3 (Bankr. N.D. W. Va. May 9, 2007). A party is not seeking an advisory opinion when "the facts alleged, under all the circumstances, show that there is a substantial controversy, between parties having adverse legal interests, of sufficient immediacy and reality." Id. (quoting Maryland Cas. Co. v. Pacific Coal & Oil Co., 312 U.S. 270, 273 (1941)).

Moreover, courts have held that a party is not seeking an advisory opinion merely by requesting that the court address threshold legal issues before making a determination on underlying facts. See Thomas v. Union Carbide Agric. Prods. Co., 473 U.S. 568, 581 (1985) ("The issue presented in this case is purely legal, and will not be clarified by further factual development . . . . 'One

does not have to await the consummation of threatened injury to obtain preventive relief. If the injury is certainly impending, that is enough.'") (citation omitted); Pac. Gas & Elec. Co. v. State Energy Res. Conservation & Dev. Comm'n, 461 U.S. 190, 201 (1983) (holding that a case is ripe for decision even though all the factual predicates ordinarily necessary for review have not been met when the question presented was predominantly legal and withholding a decision would work a substantial hardship on the parties); Satellite Broad. & Communs. Ass'n v. FCC, 275 F.3d 337, 369 (4th Cir. 2001) (holding that a case is ripe for review when it raises purely legal questions).

Here, the Debtors are requesting that the Court rule on specific threshold legal issues presented by a multitude of 503(b)(9) Claims and Responses. These legal issues are live controversies or disputes between the Debtors and the Respondents. Indeed, in the Objection, the Debtors have set forth sufficient facts to demonstrate that there is a substantial controversy between the Debtors and the Respondents, and that the parties have adverse legal interests of sufficient immediacy and reality such that there is a justiciable issue to be resolved, not an advisory opinion requested.

Third, the process the Debtors are seeking to employ fits easily within the Bankruptcy Rules. As this Court well knows, pursuant to Bankruptcy Rule 3007, a claims objection need not be made in an adversary proceeding. Moreover, upon receiving the Responses, the Objection is a contested matter governed by Bankruptcy Rule 9014. See In re Fleming, 2008 WL 4736269, * 1 (Bankr. E.D. Va. Oct. 15, 2008) (Huennekens, J.) ("The hearing on the claim objection is treated as a contested matter, and Fed. R. Bankr.P. 9014 applies."). As such, certain rules under part VII of the Bankruptcy Rules apply, including Bankruptcy Rule 7056, which incorporates Rule 56 of the Federal Rules of Civil Procedure (the "Civil Rules"). See id.; see also Fed. R. Bankr. P. 7056.

Under Civil Rule 56, a party may request partial summary judgment. See Fed. R. Civ. P. 56(a), (b) (providing that any party "may move, with or without supporting affidavits, for summary judgment on all or part claim"). Here, the Debtors have, in essence, requested partial summary judgment on certain legal issues for which no genuine issue of material fact is in dispute. Thus, the Debtors' request to bifurcate the hearings is proper under the applicable Bankruptcy Rules.

Finally, the same exact process requested by the Debtors has been followed by other bankruptcy courts in similar situations. See, e.g., In re Plastech Engineered Prods., Inc., 394 B.R. 147, 149 (Bankr. E.D. Mich. 2008) (issuing an opinion addressing whether 502(d) applied to 503(b)(9) claims without making findings as to any particular claimant); In re Leeds Bldg. Prods., Inc., 141 B.R. 265, 266 (Bankr. N.D. Ga. 1992) (implementing a bifurcated hearing process whereby threshold legal issues were resolved prior to making specific findings of fact concerning each claimant).[5] In that regard, the decision in Plastech is particularly instructive. In Plastech, the debtor requested that the court resolve the common legal issue applicable to all 503(b)(9) claimants -- whether

[5] See also In re Stegall, No. 05-09519, 2007 WL 1125635, at *1 (Bankr. S.D. Iowa Apr. 3, 2007) (noting that the court would consider the primary threshold legal issue before receiving factual information or a presentation of evidence on the merits of the parties' claims); In re Hackney, 351 B.R. 179, 181 (Bankr. N.D. Ala. 2006) (holding that the court would consider the threshold legal issue underlying a claim before it considered the claim's merits); In re Dawson, 346 B.R. 503, 507 (Bankr. N.D. Cal. 2006) (noting that the court issued a memorandum of decision addressing the underlying legal issues before resolving remaining factual issues); In re Hicks, 300 B.R. 372, 375 (Bankr. D. Idaho 2003) (holding that because a threshold legal issue emerged from the parties' arguments, the court would consider the legal issue first and reserve any evidentiary issues for a subsequent hearing); In re Lenartz, No. 01-40268, 2001 WL 35814401, at *1 (Bankr. D. Idaho May 3, 2001) (holding that before conducting an evidentiary hearing on the merits, the court would decide the underlying threshold legal issue).

section 502(d) can be raised to temporarily disallow 503(b)(9) claims based on claimants' receipt of an avoidable transfer, before issuing findings of fact concerning the application of 502(d) to each claimant. Plastech, 394 B.R. at 150. This is precisely the relief the Debtors seek here.

Therefore, the process proposed by the Debtors is appropriate and any objections thereto should be overruled.

II. THE DEBTORS ARE PERMITTED TO PROCEED BY OBJECTION AND WERE NOT REQUIRED TO COMMENCE AN ADVERSARY PROCEEDING.

A. Section 502(d) Is A Defense That May Be Raised In A Claim Objection.

In the Objection, the Debtors raised section 502(d) as a defense and did not seek to recover affirmatively any property or other amount owed to Circuit City by the Respondents. Nonetheless, certain Respondents argue that the Debtors must commence an adversary proceeding to invoke section 502(d) because raising a section 502(d) defense amounts to an action to avoid the underlying preferential transfers -- an action to recovery money or property under Bankruptcy Rule 7001(1).[6] The

[6] See Response of Pioneer at p. 5; Response of Samsung at p. 33; Response of Sandisk Corp. ("Sandisk")(D.I. 5449) at p. 3, ¶ 9.

Respondents, however, fail to cite any authority to substantiate that contention.

More importantly, that contention is inconsistent with Bankruptcy Rule 3007 and reads Bankruptcy Rule 7001 far too broadly. In particular, pursuant to Bankruptcy Rule 3007, the Debtors are permitted to object to claims. See Fed. R. Bankr. P. 3007(a) ("An objection to the allowance of a claim shall be in writing and filed."). Critically, Bankruptcy Rule 3007, not 7001, governs objections to claims. See Fed. Bankr. R. 7001 advisory committee's note (stating that "objections to claims are governed by [Bankruptcy] Rule 3007."). And, critically, by the Objection, the Debtors are not seeking any affirmative relief such as the recovery of money or property or an injunction -- that might otherwise require them to commence an adversary proceeding. See Fed. R. Bankr. P. 3007(b). Instead, the Debtors are only raising an affirmative defense to the allowance of the section 503(b)(9) Claims.

Specifically, a debtor is authorized (and in certain instances compelled) to raise defenses to claims in a claim objection. See In re Handy Andy Home Imp. Centers, Inc., 222 B.R. 571, 573-74 (Bankr. N.D. Ill. 1998) ("However, just as 'proofs of claim have been held

analogous to complaints initiating civil actions[,] an objection to a claim should meet the standards of an answer.' . . . According to Federal Rule of Civil Procedure 8(b), an answering party must 'state in short and plain terms the party's defenses to each claim and shall admit or deny the averments upon which the adverse party relies.'"(internal citations omitted)). It follows, that section 502(d) may be raised as a defense in a claim objection.

Accordingly, the Debtors were not required to commence an adversary proceeding to invoke section 502(d) to temporarily disallow the 503(b)(9) Claims.

B. The Debtors Are Not Seeking A Declaratory Judgment.

Respondents further argue that the Debtors are seeking a declaratory judgment with regard to the recovery of money or property. As such, they contend that Bankruptcy Rules 7001(1) and (9) govern the Debtors' request.[7] These Respondents, however, read Bankruptcy Rule 7001(9) too broadly, as any claim for partial summary

[7] See Response of Pioneer at p. 5; Response of Samsung at p. 33; Response of Sandisk at p. 3, ¶ 9.

judgment relief would then be considered a declaratory judgment action. It is not.

In any event, the Debtors are not seeking to recover money or property; they are asserting an affirmative defense and seeking a legal ruling that section 502(d) may be used to disallow 503(b)(9) Claims. Consequently, Bankruptcy Rule 7001(9) is inapplicable. Accordingly, the Respondents' procedural objections should be overruled.

III. SECTION 503(B)(9) ADMINISTRATIVE EXPENSES ARE SUBJECT TO MANDATORY DISALLOWANCE UNDER SECTION 502(D).

As set forth in the Opening Brief, the Debtors maintain that section 502(d) may be invoked to temporarily disallow the 503(b)(9) Claims. In support, the Debtors rely upon the clear and unambiguous language of section 502(d), its legislative history, and general policy considerations. The Respondents disagree and primarily argue that sections 501 and 502, on the one hand, and section 503, on the other, are mutually exclusive. In support, the Respondents rely on three recent court decisions -- ASM Capital, LP v. Ames Dep't Stores, Inc. (In re Ames Dept' Stores, Inc.), 582 F.3d 422 (2d Cir. 2009), Plastech, and Southern Polymer, Inc, v. TI Acquisition, LLC

(In re TI Acquisition, LLC), 410 B.R. 742 (Bankr. N.D. Ga 2009).

These three cases all concluded that section 502(d) does not apply to administrative expenses. The Ames decision, however, is distinguishable because the court was not addressing the interaction between section 503(b)(9) and section 502(d). Ames, 582 F.3d at 424, n.2 (noting that the court declined to "specifically address [section 503(b)(9)'s] interaction with section 502(d)."). Although the remaining two cases addressed the issue presented to this Court, the Debtors contend that they were wrongly decided. Moreover, in the Debtors' view those cases rested on the faulty premise that Congress intended sections 502 and 503 to be mutually exclusive and, thus, that section 502(d) only apply to claims filed under section 502, not 503. See TI Acquisition, 410 B.R. at 750 (discussing the purpose of sections 502 and 503 and concluding that section 502(d) does not apply to section 503 administrative claims); Plastech, 394 B.R. at 161 (same). As set forth in the Opening Brief and discussed below, the plain language of the Bankruptcy Code demonstrates otherwise.

Bankruptcy Code section 502(d) provides, in pertinent part, as follows:

> Notwithstanding subsections (a) and (b) of this section, the court shall disallow any claim of any entity from which property is recoverable under section . . . 550 of this title . . . or that is a transferee of a transfer avoidable under section . . . 547 . . . of this title . . . .

11 U.S.C. § 502(d).

The Debtors and certain Respondents agree[8] that when a "statute's language is plain . . . the sole function of the courts is to enforce it according to its terms." United States v. Ron Pair Enters., Inc., 489 U.S. 235, 241 (1989); see also Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A., 530 U.S. 1, 6 (2000) (stating that a fundamental principle of statutory interpretation is that "Congress 'says in a statute what it means and means in a statute what it says there'") (citation omitted). Similarly, the Debtors and certain Respondents agree that Bankruptcy Code section 502(d) is clear and unambiguous. At this point, however, the parties' agreement ends.

Section 502(d) speaks of "any claim of any entity[.]" As demonstrated in the Opening Brief, there is no basis for holding that this phrase only applies to pre-petition claims or claims for which proofs of claim are

[8] See, e.g., Response of Samsung at p. 7; Response of LG at p. 14-15.

filed, and not to pre-petition administrative expenses. See Opening Brief at 6-11 (discussing the meaning of "claim" and "entity" and distinguishing such terms from "debt" and "creditor"); see also Official Form 10 ("NOTE: This form should not be used to make a claim for administrative expenses arising after the commencement of the case.") (emphasis added).

In response, certain Respondents point to the introductory language in section 502(d), "[n]otwithstanding subsections (a) and (b) of this section[.]"[9] Relying on Ames, Plastech, and Beasley Forest Prod., Inc v. Durango Ga. Paper Co. (In re Durango Ga. Paper Co.), 297 B.R. 326 (Bankr. S.D. Ga. 2003), these Respondents contend that this clause establishes that sections 502 and 503 are mutually exclusive.[10] See Ames, 582 F.3d at 432; Plastech, 394 B.R. at 164; Durango, 297 B.R. at 330. This conclusion, however, ignores the history and application of section 502(d) and its statutory predecessor 57(d). See Opening Brief at 15-

[9] See Response of Samsung at pp. 8-10; Response of LG at pp. 14-15; Response of Toshiba America Consumer Products, LLC ("Toshiba") (D.I. 5495) at p. 7, ¶ 20.

[10] See Response of Samsung at pp. 8-13; Response of LG at pp. 12-16.

18. Moreover, it fails to appreciate why section 503(b) is likely not referenced in section 502(d).

Under section 502(a), a claim is allowed, unless it is the subject of an objection. See 11 U.S.C. § 502(b). Subsection (b) sets forth a list of objections, which must be raised by a party in interest to overcome the presumption that the claim is allowed. See 11 U.S.C. § 502(b). Thus, under section 502, the burden to overcome allowance of the claim is on the party objecting. Consequently, without introductory "notwithstanding" language, it would be unclear as to whether a claim allowed under subsection (a) and not subject to disallowance under subsection (b) could still be temporarily disallowed under subsection (d). Ames, 582 F.3d at 430 (stating that Section 502(d) avoids a [] conflict with sections 502(a) and (b) by expressly providing that it applies "[n]otwithstanding subsections (a) and (b) of this section.").

In contrast, under section 503(b), a claim is not allowed as an administrative expense until after notice and a hearing. See 11 U.S.C. § 503(b). Moreover, section 503(b) lists those claims that may be allowed as administrative expenses, see 11 U.S.C. § 503(b)(1)-(9), and

in all instances, the movant, not a party objecting, bears the burden of proof on all elements of an administrative expense. See In re Merry-Go-Round Enterprises v. Simon Debartolo Group, 180 F.3d 149, 157 (4th Cir. 1999); Ford Motor Credit Co. v. Dobbins, 35 F.3d 860, 866 (4th Cir. 1994). Thus, there was simply no reason for Congress to address section 503(b) claims in section 502(d).

Moreover, both the Respondents and the cases they rely on failed to fully consider the statutory text of sections 502 and 503. First, as discussed in the Opening Brief, section 503 expressly references section 502. Specifically, section 503(b) provides, in pertinent part, that "[a]fter notice and a hearing, there shall be allowed administrative expenses, other than claims allowed under section 502(f) of this title . . . [.]" 11 U.S.C. § 503(b) (emphasis added). If sections 502 and 503 were truly mutually exclusive, the reference to section 502(f) would be superfluous. See Opening Brief at 14. None of the three decisions cited by the Respondents considered this text in reaching the conclusion that the two sections are mutually exclusive.

Moreover, although at least one Respondent contends that such language is not superfluous, that

Respondent's argument is easily refuted.[11] Specifically, the Respondent contends that the reference to section 502(f) is meant "to clarify" that section 502(f) claims are not administrative expenses.[12] Yet, if sections 502 and 503 were mutually exclusive, there would be no need for any clarification. Thus, consistent with accepted principles of statutory construction, this Court must give effect to the language and the only way to do so, is to hold that sections 502 and 503 are not mutually exclusive.

In light of the foregoing, and for the additional reasons set forth in the Opening Brief, section 502(d) applies to all claims, including the 503(b)(9) Claims.

IV. TO INVOKE SECTION 502(D), THE DEBTORS ARE ONLY REQUIRED TO MAKE A PRIMA FACIE SHOWING THAT THE RESPONDENTS RECEIVED AN AVOIDABLE TRANSFER.

In the Opening Brief, the Debtors allege that each of the Respondents was the recipient of one or more transfers that are avoidable under Bankruptcy Code section 547 and, thus, that section 502(d) may be invoked to temporarily disallow the 503(b)(9) Claims. In response, certain Respondents contend that the Debtors have failed to

[11] See Response of Bush Industries, Inc. ("Bush") (D.I. 5505) at p. 3, ¶ 8.

[12] See id.

meet their burden under Bankruptcy Code section 502(d) because (i) the Debtors have not met their evidentiary burden with respect to alleging that each Respondent was the recipient of an avoidable transfer[13] or (ii) the Debtors are required to obtain a judgment under section 547 and 550 to invoke section 503(d).[14]

The Debtors contend that, notwithstanding these arguments, the 503(b)(9) Claims may be neither allowed nor disallowed. See In re Sierra-Cal, 210 B.R. 168, 173 (Bankr. E.D. Cal. 1997) ("[W]hile actual adjudication of the avoidance action . . . is ultimately necessary, the mere assertion of a prima facie 502(d) defense is sufficient to place the claim in a status in which it is neither allowed [n]or disallowed."); see also Katchen v. Landy, 382 U.S. 323, 330 (1966) ("Unavoidably and by the very terms of the Act, when a bankruptcy trustee presents a [section 57g] objection to a claim, the claim can neither be allowed nor disallowed until the preference matter is adjudicated.").

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[13] See Response of Paramount at p. 12; Response of Sandisk at p. 4; ¶ 10; Response of LG at p. 4.

[14] See Response of Toshiba at p. 9, ¶ 24; Response of Samsung at pp. 28-30; Response of Twentieth Century Fox Home Entertainment ("Fox") (D.I. 5504) at p. 2, ¶ 5; Response of LG at pp. 6-8. The Respondents' contention has been accepted by a minority of courts. See, e.g., In re Lids Corp., 260 B.R. 680, 684 (Bankr. D. Del. 2001).

To satisfy their burden, the Debtors submit that they are only required to allege each of the five elements set forth in section 547(b) in accordance with the liberal notice pleading requirement of Civil Rule 8(a) and the standard for dismissal under Civil Procedure 12. C.f., Official Committee of Unsecured Creditors v. Brandywine Apartments (In re the IT Group), 313 B.R. 370, 373-374 (Bankr. D. Del. 2004) (holding that debtor need not satisfy heightened pleading requirement for preference action at the motion to dismiss stage); Family Golf Centers, Inc. v. Acushnet Co., and Fortune Brands, Inc. (In re Randall's Island Family Golf Centers, Inc.), 290 B.R. 55 (Bankr. S.D.N.Y. 2003) (same). The Debtors submit that they have satisfied their burden by alleging that each Respondent was the recipient of one or more avoidable transfers. See Opening Brief at 3-4.

Certain Respondents argue that even if the Debtors could allege that they received an avoidable transfer, that is not sufficient. Instead, they contend that the Debtors are required to obtain a judgment before proceeding under section 502(d), citing Gold v. Eccleston (In re Dornier Aviation (N.Am.), Inc., 320 B.R. 831 (E.D. Va. 2005) for the proposition that section 502(d) applies

"only when a fixed amount of adjudicated preference liability remains unpaid -- not when an avoidance action has not yet been litigated."[15] Id. at 835. Although this language appears in the court's opinion in Dornier, it appears in the court's summary of one litigant's argument and is not the holding. Id.

The issue in Dornier was whether a debtor may bring a preference action after failing to object to a claim under 502(d), not whether the debtor needed to obtain a judgment prior to invoking section 502(d). Id. at 835. Thus, the court in Dornier never held that to invoke section 502(d) a debtor must first obtain a judgment of liability.[16]

In any event, the Respondents' position is simply inconsistent with the plain language of section 502(d). That section "refers to 'a transfer avoidable' rather than 'an avoided transfer' or 'claims that have been avoided'". See Enron Corp. Avenue Special Situation Fund II, L.P. (In re Enron Corp.), 340 B.R. 180, 190 (Bankr. S.D.N.Y. 2006);

[15] See Response of Toshiba at p. 9, ¶ 24; Reponse of Paramount at p. 10; Response of Fox at p. 2, ¶ 5; Response of LG at pp. 6-7.

[16] To the extent the Court did conclude that a judgment was necessary, the Debtors respectfully submit that the decision was wrongly decided.

In re Red Dot Scenic, Inc., 313 B.R. 181, 186 (Bankr. S.D.N.Y. 2004) ("[S]ection 502(d) does not even necessarily require entry of a judgment."). Thus, as the Ninth Circuit has observed, "[there would be] no purpose for section 502(d) if it applied only when the transfer therein contemplated could form the basis of an independent avoidance action." Commodity Credit Copr. V. Nat'l Dairy Promotion & Research Bd. (In re KF Dairies, Inc.), 143 B.R. 734, 737 (B.A.P. 9th Cir. 1992).

Furthermore, the Respondents' contention is at odds with those courts that have held that a debtor may invoke section 502(d) even where an avoidance action for the underlying transfer was time-barred. See id. at 736 (invoking 502(d) even where avoidance action is time-barred); U.S. Lines, Inc. v. United States (In re McLean Indus.), 184 B.R. 10, 14 (Bankr. S.D.N.Y. 1996) (same); cf. In re Eye Contact, Inc., 97 B.R. 990, 992 (Bankr. W.D. Wis. 1989) ("The trustee need not commence an avoidance action to bring section 502(d) into play."). Indeed, in such situations, no affirmative judgment as to liability could be entered and, thus, no use of section 502(d) could be made. Consequently, the Debtors are not required to obtain a judgment in order to invoke section 502(d).

Accordingly, the Debtors are only required to make a prime facie showing that each element of a preference is satisfied.

V. FACTUAL DISPUTES SHOULD BE RESERVED FOR A HEARING AFTER THE COURT RESOLVES THE THRESHOLD LEGAL ISSUES AND DISCOVERY CONCLUDES.

The Respondents raised various issues of fact in their Responses. The Debtors disagree with such factual issues, but do not intend to address such issues at the Hearing. Instead, as set forth in the Objection and this Reply, subject to the Court's approval, the Debtors have requested resolution of legal issues only. Indeed, the Debtors will not request entry of an order authorizing temporary disallowance with respect to any of the Respondents at the Hearing. Only after discovery, if any, and a subsequent hearing on the merits will the Debtors seek entry of orders resolving the Objection with respect to the Respondents.

CONCLUSION

WHEREFORE, the Debtors request the Court to enter the Order sustaining the Objection and granting such other and further relief as the Court deems appropriate.

Dated: Richmond, Virginia
November 10, 2009

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